No. 17-494

In the
Supreme Court of the United States

SOUTH DAKOTA,
Petitioner,
v.
WAYFAIR, INC., OVERSTOCK.COM, INC., AND NEWEGG, INC.,
Respondents.

On Writ of Certiorari to the
Supreme Court of South Dakota

BRIEF OF *AMICI CURIAE* MULTISTATE TAX COMMISSION AND FEDERATION OF TAX ADMINISTRATORS IN SUPPORT OF PETITIONER

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INTEREST OF THE *AMICI CURIAE*

The Multistate Tax Commission (Commission) and the Federation of Tax Administrators (Federation) respectfully submit this brief as *amici curiae* in support of South Dakota, urging the Court to overturn *Quill* and permit states to adopt workable nexus standards for imposing sales and use tax collection requirements.[1]

The Commission is an intergovernmental state tax agency created by the Multistate Tax Compact and composed of the state tax agency heads of the states that are a party to the Compact. Other states participate in Commission activities as Sovereignty or Associate members.[2] The Commission's purposes include facilitating the determination of

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[1] No counsel for any party authored this brief in whole or in part. Only *amici curiae* Multistate Tax Commission and Federation of Tax Administrators and their member states, through the payment of their membership fees, made any monetary contribution to the preparation or submission of this brief. This brief is filed by the Commission and the Federation, not on behalf of any particular member state other than South Dakota. Counsel of record for the parties have filed blanket consents to the filing of *amicus* briefs.

[2] *Compact members* are: Alabama, Alaska, Arkansas, Colorado, District of Columbia, Hawaii, Idaho, Kansas, Missouri, Montana, New Mexico, North Dakota, Oregon, Texas, Utah, and Washington. *Sovereignty members* are: Georgia, Kentucky, Louisiana, Michigan, Minnesota, New Jersey, Rhode Island, and West Virginia. *Associate Members* are: Arizona, California, Connecticut, Delaware, Florida, Illinois, Indiana, Iowa, Maine, Maryland, Massachusetts, Mississippi, Nebraska, New Hampshire, New York, North Carolina, Ohio, Oklahoma, Pennsylvania, South Carolina, South Dakota, Tennessee, Vermont, Wisconsin, and Wyoming.

tax liabilities of multistate businesses, promoting uniformity or compatibility in state tax systems, fostering taxpayer convenience and compliance, and avoiding duplicative taxation.[3] The Commission's principal activities include drafting model state tax laws, conducting joint state tax audits, and providing a "one-stop" program for multistate businesses to voluntarily disclose and settle unreported state tax liabilities.[4]

The Federation is the membership organization for state revenue agencies. Previously known as the National Association of Tax Administrators, the Federation has been operating since 1937. The members of the Federation are all 50 states, the District of Columbia, and the cities of New York and Philadelphia. The primary purpose of the Federation is to promote best practices in state tax administration and tax enforcement. The Federation accomplishes this purpose primarily through educational, information-sharing, and other cooperative programs.[5]

The Federation and the Commission have overlapping membership and similar goals. Moreo-

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[3] *See* Art. I of the model Multistate Tax Compact, *available at*: http://www.mtc.gov/getattachment/The-Commission/Multistate-Tax-Compact/Original-Model-Multistate-Tax-Compact.pdf.aspx (last visited March 1, 2018).

[4] Information on the Commission's programs and committees is at http://www.mtc.gov/.

[5] Information on the Federation and its activities is available on its website, at https://www.taxadmin.org/.

ver, the Commission's history is bound up with the Court's shifting dormant commerce clause and state tax nexus jurisprudence.[6] In 1959, after this Court held in *Northwestern States Portland Cement Co.*[7] that states could impose apportioned state income taxes on out-of-state businesses soliciting sales in those states, various groups urged Congress to step in. States responded by simplifying aspects of their tax systems and by forming the Commission. Eventually, this Court decided *Complete Auto*,[8] affirming *Northwestern States*, and rejecting, once and for all, the idea that interstate commerce is immune from its just share of fairly imposed state taxes.

Arguably, no organizations have a greater focus on the fair, effective administration and enforcement of state taxes than the Commission and the Federation. Therefore, this case is of the utmost interest to your *amici*.

SUMMARY OF ARGUMENT

Nat'l Bellas Hess, Inc. v. Dep't of Revenue of State of Ill., 386 U.S. 753 (1967) and *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992) adopted a physical-presence test as a bright-line nexus standard for imposing state sales and use tax collection obligations. Today, physical presence, as a test, no longer

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[6] *See U.S. Steel Corp. v. Multistate Tax Comm'n*, 434 U.S. 452, 555-556 (1978).

[7] *Northwestern States Portland Cement Co. v. Minnesota*, 358 U.S. 450 (1959).

[8] *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274 (1977).

creates a very bright line, but more troublingly, it bears so little relationship to the relative burdens of state tax collection that it leads to irrational results.

The *Quill* Court acknowledged that the physical presence standard was out of step with the modern dormant commerce clause doctrine. It nevertheless declined to change the standard, citing two collateral concerns—that overturning *Bellas Hess* would subject sellers to retroactive liabilities, and that the Court's due process analysis in *Bellas Hess* might have prevented Congress from changing the standard prospectively. The respondents here raise a third concern—that states will abuse any authority they are given to adopt alternative nexus standards. But if physical presence has become unworkable as a test for substantial nexus, it can be discarded without disturbing sellers' reliance interests, or altering Congress's ability or authority to act. Nor will this give the states any power other than to implement reasonable, workable alternative standards.

ARGUMENT

I. Fundamental dormant commerce clause doctrines evolve when necessary; so too should a test meant to serve those doctrines.

A. Under the modern dormant commerce clause doctrine, the role of the physical presence nexus standard in *Quill* is to serve as a test for undue burdens.

Interpretations of the dormant commerce clause doctrine and its restrictions on state taxes, have, in the words of the *Quill* Court, "evolved substantially." *Quill Corp. v. N. Dakota*, 504 U.S. 298, 309 (1992). Under the doctrine's original interpretation, the Court struck down nondiscriminatory state taxes imposing only insubstantial, incidental burdens on interstate commerce. *See Brown v. State of Maryland*, 25 U.S. 419 (1827)(striking Maryland's even-handed license tax as applied to out-of-state wholesalers bringing their wares into the state), and *Oklahoma Tax Comm'n v. Jefferson Lines, Inc.*, 514 U.S. 175, 180 (1995)(describing other early restrictive interpretations). But under the doctrine's modern interpretation, the same sorts of taxes are regularly upheld, even when the burdens imposed on interstate commerce are direct and substantial, as long as they are not "undue." *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274 (1977)(overruling *Spector Motor Service v. O'Connor*, 340 U.S. 602 (1951)). This evolution in the interpretation of the dormant com-

merce clause undoubtedly kept the states from becoming mere vestiges of our federal system. It also proved that interstate commerce can bear the burdens of fairly imposed state taxes and still thrive.

The physical presence test was adopted as a nexus standard in this area "in the middle of [the Court's] latest rally between formalism and pragmatism," and is not necessarily dictated by "contemporary Commerce Clause jurisprudence." *Quill* at 310–11. The test was derived from the Court's observations, in 1967 and 1992, of the "sharp distinction" between the burdens that tax collection imposed on two business models used in the mail-order industry—one employing "retail outlets, solicitors, or property within a State," and one "do[ing] no more than communicat[ing] with customers in the State by mail or common carrier." *Quill* at 307. Physical presence was intended to function as a "bright-line" test and, critically, to substitute for case-by-case "evaluation of the actual burdens" that sales tax collection might impose on particular sellers. *Quill* at 314. The test has not been adopted as a nexus standard for other types of taxes, *Quill* at 317, nor do the states generally apply it as a standard for other taxes.[9]

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[9] See cases rejecting the physical presence test as applying outside of the sales tax collection context which include, among others: *Geoffrey, Inc. v. South Carolina Tax Comm'n*, 437 S.E.2d 13 (S.C. 1993)(*cert. denied*, 510 U.S. 992 (1993)); *Couchot v. State Lottery Comm'n*, 659 N.E.2d 1225 (Ohio 1996)(*cert. denied*, 519 U.S. 810 (1996)); *General Motors Corp.*

B. As a bright-line test for undue burdens, sales volume thresholds are much more workable than physical presence.

This Court's modern interpretation of the dormant commerce clause no longer treats interstate commerce as immune from state tax burdens generally, including state sales and use tax collection requirements. So, for example, a seller operating almost entirely outside the state, with only a small contract sales force in the state, can be subjected to tax collection obligations on sales made into the state. *Scripto, Inc. v. Carson*, 362 U.S. 207 (1960)(where the Court reasoned that the sales force's "effectiveness in securing a substantial flow of goods" into the state also demonstrated that the nexus was substantial). And, a state may tax sales made by the mail-order division of a business where that business's only physical presence in the state is

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v. City of Seattle, 25 P.3d 1022 (Wash. Ct. App. 2001)(*cert. denied*, 535 U.S. 1056 (2002)); *A&F Trademark, Inc. v. Tolson*, 605 S.E.2d 187 (N.C. Ct. App. 2004)(*cert. denied*, 546 U.S. 821 (2005)); *Kmart Corp. v. Taxation & Revenue Dep't*, 131 P.3d 22 (N.M. 2005); *Tax Comm'r v. MBNA Am. Bank, NA*, 640 S.E.2d 226 (W. Va. 2007)(*cert. denied*, 551 U.S. 1141 (2007)); *Lanco, Inc. v. Director, Div. of Taxation*, 908 A.2d 176 (N.J. 2006)(*cert. denied*, 551 U.S. 1131 (2007)); *Capital One Bank v. Comm'r of Revenue*, 899 N.E.2d 76 (Mass. 2009)(*cert. denied*, 557 U.S. 919 (2009)); *KFC Corp. v. Iowa Dep't of Revenue*, 792 N.W.2d 308 (Iowa 2010)(*cert. denied*, 565 U.S. 817 (2011)); *Lamtec Corp. v. Dep't of Revenue*, 246 P.3d 788 (Wash. 2011)(*cert. denied*, 565 U.S. 816 (2011); *Crutchfield Corp. v. Testa*, 88 N.E.3d 900 (Ohio 2016); *ETC Mktg., Ltd. v. Harris Cty. Appraisal Dist.*, 528 S.W.3d 70 (Tex. 2017)(*cert. denied*, 138 S. Ct. 557 (2017)).

unrelated to the mail-order division. *Nat'l Geographic Society v. California Bd. of Equalization*, 430 U.S. 551 (1977). In short, the Court has long held that sales and use tax collection requirements do not impose "undue" burdens on interstate commerce generally.

The *Quill* Court, however, made this statement, which has plagued those who seek to understand the rationale for its holding: "Undue burdens on interstate commerce may be avoided not only by a case-by-case evaluation of the actual burdens . . . but also, in some situations, by the demarcation of *a discrete realm of commercial activity* that is free from interstate taxation." *Quill* 314–15 (emphasis added). This statement could be read to mean that any bright-line rule will suffice, so long as the "discrete realm" that it carves out for protection is sufficiently large enough to adequately reduce the *total* burden on interstate commerce. But even if such an indiscriminate rule might have a positive effect on commerce, there is no reasonable interpretation of the dormant commerce clause that would support it. "It was not the purpose of the commerce clause to relieve those engaged in interstate commerce from their *just share* of state tax burden even though it increases the cost of doing the business." *Western Live Stock v. Bureau of Revenue*, 303 U.S. 250, 254 (1938)(emphasis added). It is impossible to impose a "just share" of state tax burdens on interstate commerce if a "discrete realm of commercial activity" is arbitrarily excluded. "Undue" burdens cannot, therefore, refer to some excess quantity of the total bur-

den imposed on interstate commerce. Rather, if burdens that are otherwise generally permissible may become "undue," it must be because, under the particular circumstances, they significantly exceed, in relative terms, the normal burdens.

The parties in this case and their *amici* dispute whether the overall burden of sales tax collection has gone up or gone down since 1992. We believe there are significant reasons to conclude that the overall burden has gone down. But whether it has gone up, or down, or stayed the same, there is no justification for granting an indiscriminate exemption from that burden.

As for the relative burden of tax collection, it is most closely related to the seller's volume of sales. In large part, this is because there are certain "fixed" costs of tax collection and remittance, that is, costs that must be incurred regardless of the volume of sales. Spreading these fixed costs across a higher volume effectively reduces the relative cost per sale. For very small sellers, these fixed costs alone may be prohibitive. For larger sellers, however, they simply become a very minor cost that can be covered by the price charged for goods sold.

The volume of sales in a state is also an indicator of the overall size of the seller, which also affects a seller's ability to undertake certain compliance-related tasks. For example, a small seller may have too few employees to take on the additional tasks of handling a tax audit, and might therefore

have to hire additional staff. A larger seller, by contrast, may have more flexibility to handle such tasks because it has more employees whose duties can be shifted, as necessary.

Of course, no single standard, whether it is sales volume or physical presence, will be a perfect substitute for a case-by-case, factual analysis of the actual burdens imposed on particular sellers. Smaller sellers might actually have relatively low burdens in some cases. For example, the relative burden of determining the taxability of sales might be lower for a small seller with a much narrower product line compared to a somewhat larger seller that has a much more diverse product line. Similarly, the relative burden on a small seller making sales within a limited region would be lower than the burden on a somewhat larger seller making sales nationally. A nexus standard that uses a sales threshold, therefore, might tend to protect a number of smaller sellers whose overall tax collection burdens would actually be relatively low in comparison to somewhat larger sellers. But today, using physical presence as a test for nexus creates the opposite problem. Rather than overprotecting smaller sellers, it overprotects very large ones.

There was a time when physical presence was a more accurate predictor of whether a seller might have significant sales (and therefore a lower relative burden) in a particular state. Indeed, throughout most of our history, it was virtually impossible for sellers to contact potential customers, transact sales,

or deliver products without some physical presence in a state. And even as late as 1992, when mail-order was the business model for remote sales, the burdens imposed could be qualitatively different because the calculation of the tax generally had to be done by the mail-order customer, paying by check, rather than by the seller, as would be the case in a face-to-face transaction.

But today, physical presence does not dictate or even accurately predict a seller's volume of sales in a state. Nor do the same qualitative differences in burdens exist today due to the technology that facilitates calculating, charging, and collecting tax on orders made remotely. As amply demonstrated by the respondents in this case, it is possible for sellers to have millions of dollars of sales into a state, even a small state, without having any physical presence there. Exempting such sellers from any sales tax collection obligations, while imposing the same obligations on much smaller sellers operating by more traditional means, does not result in the imposition of a "just share" of those tax collection burdens on interstate commerce. The physical presence standard may very well reduce the total burden of state tax collection on interstate commerce, but it does so in an increasingly indiscriminate fashion. In sum, the physical presence standard must evolve.

II. Physical presence, as a test for sales and use tax nexus, not only produces irrational results, but is increasingly incapable of providing a predictable bright line.

Not only does physical presence fail to yield rational results, as noted above, but numerous examples demonstrate that the physical presence standard fails to produce consistent results, especially where the type of presence at issue is something other than the "retail outlets, solicitors, or property" that marked the difference between traditional mail-order sellers' primary business models. For example, courts have reached conflicting judgments as to when intermittent contacts are sufficient to create nexus. *Compare Orvis Co. v. Tax Appeals Tribunal*, 654 N.E.2d 954 (N.Y. 1995), *cert. denied*, 516 U.S. 989 (1995)(nexus established by 19 customer visits on an average of four times a year), *with In re Intercard, Inc.*, 14 P.3d 1111 (Kan. 2000)(nexus not established by 11 in-state installation visits to the company's largest in-state customer over three month period). Courts have also differed on the extent to which third parties can create nexus for sellers, even in virtually identical circumstances. For example, some courts have held that teachers taking orders for a book club seller can create nexus for that seller. *See In re Appeal of Scholastic Book Clubs, Inc.*, 920 P.2d 947 (Kan. 1996), *Scholastic Book Clubs, Inc. v. State Bd. of Equalization*, 255 Cal. Rptr. 77 (Cal. Ct. App. 1989), and *Scholastic Book Clubs, Inc. v. Farr*, 373 S.W.3d 558 (Tenn. Ct. App. 2012), *cert. denied*, 133 S.Ct. 663 (2012). But other courts have held that

teachers taking orders for a book club do not create nexus. *See Scholastic Book Clubs, Inc. v. State, Dep't of Treasury, Revenue Div.*, 567 N.W.2d 692 (Mich. Ct. App. 1997), *appeal denied* 586 N.W.2d 923 (Mich. 1998), *Pledger v. Troll Books, Inc.*, 871 S.W.2d 389 (Ark. 1994). Courts have also differed on whether affiliated entities can create nexus for each other. *Compare New Mexico Taxation & Revenue Dep't v. Barnesandnoble.com LLC*, 303 P.3d 824 (N.M. 2013); and *Borders Online, LLC v. State Bd. of Equalization*, 129 Cal.App.4th 1179 (Cal. Ct. App. 2005) (in-state affiliate created nexus for remote seller); *with SFA Folio Collections, Inc. v. Bannon*, 585 A.2d 666 (Conn. 1991); *SFA Folio Collections, Inc. v. Tracy*, 652 N.E.2d 693 (Ohio 1995); and *Bloomingdale's By Mail, Ltd. v. Commonwealth, Dep't of Revenue*, 567 A.2d 773 (Pa. Commw. Ct. 1989). So if the physical presence standard has, indeed, minimized the need for case-by-case analysis of actual burdens, it has substituted a similarly difficult case-by-case analysis of the exact type of physical presence a seller has in a state.

Every year, Bloomberg BNA publishes a multi-state report surveying state revenue agencies on their administrative policies with respect to sales tax nexus and other matters. 2017 Survey of State Tax Departments, Special Multistate Tax Report, Vol. 24, No. 4, Bureau of Nat'l Affairs, Inc. The most recent report listed the following instances where states substantially diverged in their answers to whether an out-of-state company had created sales

and use tax nexus based solely on a particular circumstance, including:

- Seller uses returnable containers to deliver products, *id.* at S-386-88;
- Seller attends trade shows, *id.* at S-390-93;
- Seller meets with instate suppliers, *id.*;
- Seller uses third-party warranty servicers, *id.* at S-394-97;
- Seller uses an in-state company to make drop-shipments of goods, *id.*;
- Seller maintains an Internet link with an in-state third-party which has a website and is paid each time the seller's ad is displayed ("per impression" agreements), *id.* at S-410-12;
- Seller uses a paid web-hosting provider with an instate server, *id.* at S-414-16;
- Seller sells software licenses, *id.* at S-418-20;
- Seller sells data that is located on a server within the state, *id.* at S-422-24;
- Seller picks up raw materials in the state, *id.* at S-426-28;
- Seller travels into the state between 6-12 times, or more than 12 times, other than to pick up or deliver goods, *id.*;
- Seller holds title to electricity or natural gas flowing through the state, *id.* at S-430-32;
- Seller hires a third party in the state to distribute physical or electronic promotional materials to potential customers, *id.* at S-434-36;

- Seller hires a third party in the state to solicit sales by telephone, *id.*;
- Seller hires a third party in the state to negotiate to buy products in the state, *id.* at S-438-40;
- Seller has agreement with instate third party with a website that refers customers to the seller through a link on that website, *id.*;
- Seller has franchise agreement with third party in the state and makes between 1-6 inspection visits per year, *id.* at S-442-44;
- Seller is out-of-state manufacturer that uses a distributor with nexus in the state to take orders which are then delivered by common carrier, *id.* at S-462-63; and
- Seller is an out-of-state distributor that uses its instate manufacturer to deliver products to customers, *id.*

These examples demonstrate how little definitive guidance the physical presence standard provides in today's marketplace.

Nevertheless, despite its questionable pedigree, growing deficiencies, and the existence of at least one superior alternative, the physical presence standard persists, while more fundamental dormant commerce clause precedents have become extinct. This appears to be due to three collateral concerns, not related to the standard itself, but to the possible effects that overturning *Quill* and *Bellas Hess* might have. We address these concerns in Section III.

III. Collateral concerns do not justify retaining physical presence as a nexus standard.

A. The reliance interests of sellers need not be disturbed if the Court determines that the physical presence test has become unworkable as a test for undue burdens.

In *Quill*, the North Dakota Supreme Court, citing "wholesale changes" in the economy and the law, declined to apply *Bellas Hess*. *Quill* at 303. Accordingly, before this Court, the state argued that *Bellas Hess* had been, or should be, overruled. This Court, however, noted that the two cases were "indistinguishable" *Id.* apparently referring to the relevant aspects of the mail-order businesses involved. It is not surprising, therefore, that the physical presence test, derived from the facts in *Bellas Hess*, was still considered workable when applied to the facts in *Quill*. *Id.* at 320 (Scalia, J. concurring). Nor is it surprising that the Court, in considering what it would mean to overrule *Bellas Hess*, might struggle to reconcile the reliance interests of the mail-order industry, *id.* at 317, with the general principle that its rulings are to be given retroactive effect. *See James B. Beam Distilling Co. v. Georgia*, 501 U.S. 529 (1991); and *Harper v. Virginia Dep't of Taxation*, 509 U.S. 86 (1993).

The *Quill* Court characterized the "substantial reliance" on the physical presence rule as having become part of the "basic framework of a sizable industry." *Quill* at 317. Of course, a bright-line test, the

very purpose of which is to substitute for the case-by-case determination of actual burdens, will naturally engender much stronger reliance interests than a more contextual inquiry into the particular facts of a given case. Such bright-line tests may, therefore, not be susceptible to incremental adaptation, even as they become obsolete. This is their inherent weakness.

It has been said that "prospective decisionmaking is incompatible with the judicial role, which is to say what the law *is*, not to prescribe what it *shall be*." *Am. Trucking Associations, Inc. v. Smith*, 496 U.S. 167, 201 (1990)(Scalia, J. concurring)(emphasis added). But we believe the physical presence standard not only represents what the *law* is, but acts as a substitute for a determination of what the *facts* are ("actual burdens"). If so, then the Court may simply remove the physical presence standard and allow the weighing of actual burdens, as a factual matter, to proceed in all cases. That weighing, of course, can occur not only in the courts, but through administrative and legislative processes. And to the extent those administrative and legislative processes arrive at a reasonable assessment of the relative burdens, and provide reasonable standards to avoid undue burdens, those standards can be applied as well.

It has also been said: "If governing decisions are unworkable or are badly reasoned, this Court has never felt constrained to follow precedent." *Payne v. Tennessee*, 501 U.S. 808, 827

(1991)(internal citations omitted). This oft-cited passage from *Payne* clearly contemplates two different rationales for overturning precedent. We have not argued that *Complete Auto's* substantial nexus requirement was badly reasoned, or even that its purpose of reducing undue burdens cannot be served by an appropriate bright-line test. We have simply argued that *Quill's* specific bright-line test, still considered workable in 1992, no longer bears any clear relationship to the burdens it is meant to address, so as to be able to discern between allowable and undue burdens. In essence, the physical presence test has become a poor standard, or stand-in, for a necessary factual determination. If the Court agrees that the standard can no longer serve as a reliable test for undue burdens on out-of-state Internet sellers or other businesses engaging in electronic commerce, then it would simply be irrational to make such a holding retroactive unless the Court can determine at what point in time the physical presence test ceased to work.

Nevertheless, if the Court determines that the physical presence standard can be altered only by retroactively overruling *Quill*, then we respectfully submit that the Court must retroactively overrule *Quill*. As we discuss further below, the Court may not retain a standard that unreasonably limits state sovereign authority to impose tax collection obligations simply because of reliance interests engendered by that standard. Of course, by declining to make its ruling prospective, the Court would not necessarily subject remote sellers to past tax liabili-

ties. That will be a matter for the states to determine. And we expect that many states cannot or will not impose such retroactive liabilities.

B. This Court cannot justify retaining a dormant commerce clause standard that unreasonably restricts state authority because Congress may have unexpressed intent regarding that standard.

The *Quill* Court removed any doubt as to Congress's power to change the physical presence standard, saying: "[Congress's] decision not to take action in this direction may, of course, have been dictated by respect for our holding in *Bellas Hess* that the Due Process Clause prohibits States from imposing such taxes, but today we have put that problem to rest." *Quill* at 318 (1992). The Court's interest in putting "that problem to rest" is no mystery. Not only did the Court hope Congress might be able to better weigh the relevant burdens, but its enactments, unlike the Court's rulings, are generally given prospective effect. Thus, Congress could change the nexus standard without disturbing mail-order sellers' reliance interests. *Id.* But as we have argued, a ruling that the physical presence standard has become unworkable as a substitute for a factual determination is the type of ruling that inherently requires it be given prospective effect.

As for Congress being better able to weigh the burdens of state tax collection on interstate commerce, nothing the Court does in this case will

change the fact that "Congress remains free to disagree with [the Court's] conclusions." *Quill* at 318.

But this does not absolve the Court. If the physical presence standard restricts state authority in a way not supported by a reasonable interpretation of the dormant commerce clause, the Court cannot simply leave it in place, waiting for Congress to remove that restriction.

> What is absolutely clear, affirmed by the text of the 1789 Constitution, by the Tenth Amendment ratified in 1791, and by innumerable cases of ours in the 220 years since, is that there are structural limits upon federal power—upon what it can prescribe with respect to private conduct, and upon what it can impose upon the sovereign States.

Nat'l Fed'n of Indep. Bus. v. Sebelius, 567 U.S. 519, 647 (2012)(Scalia, J., dissenting). The Court it is no less constrained by these structural limits upon federal power when it interprets the dormant commerce clause. While it is generally true that Congress can restore, by statute, any constitutional right unreasonably restricted by this Court's precedent, few would find that comforting.

Moreover, the requirements of the dormant commerce clause, and the substantial nexus prong of *Complete Auto*, which only this Court can speak to,

are issues that have ongoing application beyond this case. For years after *Quill*, states were uncertain whether the physical presence standard applied outside the sales tax collection context. The Court never addressed that issue, despite many opportunities, but state courts have had to grapple with it.[10] In fact, in the 25 years since *Quill*, this Court has not issued another opinion on what constitutes a substantial nexus with a state for any type of tax imposition. State lawmakers are currently considering whether to impose other obligations related to sales tax enforcement, such as information reporting, *see Direct Mktg. Ass'n v. Brohl*, 814 F.3d 1129 (10th Cir. 2016), *cert. denied*, 137 S. Ct. 593 (2016)), which involve questions of substantial nexus. Also, state courts are continuing to grapple with how substantial nexus applies to other taxes. See *Crutchfield Corp. v. Testa*, 88 N.E.3d 900 (Ohio 2016). In these and other areas, questions concerning the general requirements of substantial nexus would benefit from the Court's guidance.

Some may also argue that Congress's silence itself indicates its intent to leave the physical presence standard untouched. Silence, however, provides no reliable clue as to Congress's intent, as Justice Rutledge explained:

> There are vast differences between legislating by doing nothing and legislating by positive enactment, both in

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[10] See fn. 6 *supra*.

> the processes by which the will of Congress is derived and stated and in the clarity and certainty of the expression of its will. ... The danger of imputing to Congress, as a result of its failure to take positive or affirmative action ... is illustrated most dramatically perhaps by the vacillating and contradictory courses pursued in the long line of decisions imputing to 'the silence of Congress' varied effects in commerce clause cases.

Cleveland v. United States, 329 U.S. 14, 22–24 (1946)(Rutledge, J. concurring).

We must, however, address one specific action Congress *has* taken—the Internet Tax Freedom Act (ITFA).[11] One of the respondents' *amici* argues that ITFA's anti-discrimination provision was intended to, and can be interpreted to, preempt the action taken by South Dakota in this case. *See Brief of Chris Cox, Former Member of Congress and Co-Author of the Internet Tax Freedom Act, As* Amicus Curiae *in Support of Respondents.*[12] We do not credit this argument, nor do we agree that the interpreta-

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[11] ITFA was made permanent in Pub. L. No. 114–125, § 922(a), 130 Stat. 281, on February 24, 2016 (codified at 47 U.S.C. § 151 note).

[12] *Available at* https://www.supremecourt.gov/DocketPDF/17/17-494/23030/20171207151532703_Amicus%20Brief.pdf (last visited Feb. 25, 2018)

tion is a reasonable reading of the statutory text. The anti-discrimination provision prohibits differential tax treatment of transactions that are essentially identical except that one is made over the Internet. The asserted interpretation, in contrast, compares transactions that are factually different in other ways. *Id.* at 11–12. Indeed, this same interpretation, if applied to existing state law, would preempt sales taxes currently imposed, yet we are not aware of any case that has argued for or any court that has held that the anti-discrimination provision may be interpreted in this way. We also note that Wayfair does not assert that ITFA preempts South Dakota's action here.

Finally, we must respond to the *Quill* Court's assertion that the issue in this case is one that Congress "may be better qualified to resolve," *Quill* at 318. That Congress is the proper institution to address this issue was also the chief argument made by the respondents in their Brief in Opposition to Writ of Certiorari (see p. 9). It was also, notably, a sentiment expressed by those who long opposed the evolution of the Court's dormant commerce clause doctrines and the loosening of its perceived restrictions on the states. As Justice Frankfurter, a chief opponent of the modern dormant commerce clause, expressed in his dissent in *Northwestern States Portland Cement*: "The question is not whether a fair share of the profits derived from the carrying on of exclusively interstate commerce should contribute to the cost of the state governments. The question is whether the answer to this problem rests *with this*

Court or with Congress." Northwestern States Portland Cement Co. v. Minnesota, 358 U.S. 450, 475 (1959)(Frankfurter, J. dissenting)(emphasis added).

Conspicuously missing from this formulation of the question is any mention of the role of the states. Nor is that surprising. Those who oppose the imposition of state tax requirements naturally cast the states as a problem to be solved by the federal government, rather than important participants in our federal system. But relegating the states to petitioning Congress for relief, and assuming that this resolves any interests they may have, simply ignores "the tactical advantage *Quill* bestows in the political process upon the Internet and mail-order industries," and "the unique disadvantages of the states in the federal legislative process."[13]

The states cannot be faulted if they view the lack of congressional action as an indication that they simply lack the clout to obtain any change. The Federation, which had a long-standing resolution advocating for a Congressional solution, has recently recognized this reality and, in 2017, it resolved as follows:

> Decades of good-faith effort has generated no meaningful progress by Con-

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[13] Edward A. Zelinsky, *The Political Argument for Overruling* Quill, 82 Brook. L. Rev. 1177, 1178 (2017), *available at* https://brooklynworks.brooklaw.edu/cgi/viewcontent.cgi?referer=&httpsredir=1&article=1551&context=blr (last visited Feb. 27, 2018).

> gress toward the goal of developing a workable solution for all stakeholders related to the issue of remote seller collection authority. At this time, it appears that any federal legislation could contain unacceptable language that limits state taxing authority. Therefore, FTA supports the right of any state to enact fair and reasonable laws related to remote seller collection authority and to test the limits of, or seek to overturn, the *Quill* decision.

Federation of Tax Administrators Resolution 2017-1: Remote Seller Collection Authority, *available at* https://www.taxadmin.org/assets/docs/AssocDocs/2017-1.pdf (last visited March 1, 2018).

C. Revision of the sales tax nexus standard can be accomplished without the states imposing undue burdens, nor do they have any interest in imposing such burdens on interstate commerce.

Respondents and their *amici* also speculate about a parade of horribles that will come to pass if states are given the authority to replace the physical presence standard. We address certain specific concerns below.

1. *Adoption of unreasonably low thresholds.* Taking into account South Dakota's small population, its sales-threshold standard of $100,000 (or 200 sales)

will exempt most small and even some medium-sized sellers from having to collect sales tax. Even small states have reasons to refrain from imposing an unduly low threshold standard. First, a substantial portion of total sales made will be exempt, either as sales for resale or for some other reason, so that a substantial percentage of total sales will not generate any tax. Second, states will, themselves, incur costs to register, track, process returns, and provide notices to small sellers, that, like the fixed costs of compliance, make imposing tax collection obligations on small sellers inefficient from the states' standpoint. In addition, small start-up businesses cease operations with greater frequency and, when this happens, it is generally incumbent on a state administrator to follow up to determine why the seller has stopped filing reports and then cancel the seller's registration and annotate any agency files. Other enforcement and collection actions are even more costly, especially when the business has no physical presence in the state, and resources for such actions are limited.

2. *Adoption of different state thresholds.* Not only is it preferable to allow states to vary the amount of the sales-threshold standard, it might actually increase overall burdens to impose a national standard. States may vary their standard based, in part, on their population or other relevant factors such as whether or not the state provides simplified methods of compliance or allows "vendor collection discounts"

to offset the sellers' costs.[14] Based on these factors, states may determine that they wish to have a standard that would be higher than an equivalent national standard would be. Nor is it possible for a national standard to reflect all the state-specific factors that may be relevant. Moreover, even an effectively equivalent national standard would not impose a lower burden since, presumably, a seller that exceeded that national standard would be required to collect and remit tax in every state into which it had sales, even in states where its total sales are minimal.

3. *The administrative rules to implement sales thresholds do not exist.* Administrative rules are necessary to implement sales thresholds, just as they have been necessary to implement the physical presence standard. But in comparison to physical presence, sales thresholds would be simpler to administer. Moreover, most of the necessary rules, including rules for sourcing of sales to particular states, already exist. Indeed, these sourcing rules, that generally look to the destination to where the goods are shipped or services are performed, are necessary to impose the tax. Sales-threshold standards offer another advantage over physical presence, in terms of practical application. A seller's physical contacts

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[14] 30 states currently provide these discounts to vendors to compensate them for the time and expense incurred in collecting the tax on behalf of state and local jurisdictions. The discount is usually provided by allowing the vendor to retain a percentage of the amount collected that is to be remitted for tax payment.

may change from *de minimis* to substantial in a matter of days, causing the seller to become subject to tax in a current reporting period, whereas a seller will have more notice that its sales have exceeded (or may exceed) sales-threshold standards in some earlier measuring period.

4. *Smaller sellers will be subjected to audits.* Audits serve an important administrative function. Their purpose is not to harass taxpayers, but to ensure a level of compliance with a system that is otherwise entirely voluntary. But the chance of a small seller being subjected to regular audit is extremely small. State audit resources are limited, and any audit that is likely to be unduly expensive for the taxpayer, given its size and amount of sales, will also be unduly expensive for the state. If, on average, taxes are underreported by ten percent, then assuming the tax rate is eight percent, an audit of a seller making $1 million in sales into the state will generate, on average, only $8,000. Of course, some taxpayers may underreport by much more than the average rate. Where a state has information that taxpayer has underreported by 50 percent, for example, this would likely increase that taxpayer's chance of being audited, as it should. But, it is also true that states have other ways of dealing with apparent underreporting, besides full-fledged audits, which reduce the administrative costs for both the state and the taxpayer. Moreover, even the low rate of audits of in-state sellers is likely to overstate the chance that an out-of-state seller will be audited since in-state sellers are sometimes audited for additional purposes, in-

cluding to determine if they have paid use tax on equipment used in the state or have properly withheld taxes on employees working in the state.

5. *Sales thresholds will generate litigation and will burden the courts.* While we believe the implementation of sales-threshold nexus standards should be fairly straightforward, it is possible that there may be challenges to those standards or their application in particular circumstances. But the physical presence standard generated substantial litigation over the last 25 years, although none of those cases ever reached this Court. There is no reason to expect that litigation over sales thresholds will be any greater burden on state courts, or on this Court.

CONCLUSION

The physical presence nexus standard for state sales and use tax collection is no longer suited to the purpose of distinguishing undue burdens on interstate commerce. That nexus standard must, therefore, evolve. Your *amici* submit that this evolution can be accomplished by holding that the standard has become unworkable and granting states the authority, through their legislative and regulatory processes, to adopt more appropriate standards. This need not disturb sellers' reliance interests, nor will it affect the ability of the courts or Congress to ensure that states do not abuse that authority.

Respectfully submitted,

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